SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1944

No. 932

TRUST U/W OF MARY LILY (FLAGLER) BINGHAM, MESSRS. WILLIAM R. KENAN, JR., AND LAWRENCE C. HAINES, TRUSTEES, PETITIONER,

vs.

COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

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[fol. 1]

BEFORE UNITED STATES BOARD OF TAX APPEALS

Docket No. 109384

TRUST U/W OF MARY LILY (FLAGLER) BINGHAM, Messrs William R. Kenan, Jr., and Lawrence C. Haines, Trustees, petitioners

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Appearances: For Taxpayer: (Withdrawn), Geo. E. Cleary, Esq., S. Milton Simpson, Esq. For Comm'r: Thos. H. Lewis, Jr., Esq.

1941 DOCKET ENTRIES

Dec. 11—Petition received and filed. Taxpayer notified. Fee paid.

Dec. 11—Copy of petition served on General Counsel.

Dec. 11—Notice of appearances of A. Roberts MacMannis as counsel filed. 12-11-41. Copy served.

Dec. 31—Answer filed by General Counsel.

Dec. 31—Request for hearing in New York filed by General Counsel.

1942

Jan. 5—Notice issued placing proceeding on New York City calendar. Service of answer and request made.

Dec. 21—Hearing set Jan. 25, 1943, New York City.

Dec. 26—Motion for continuance of 17 days filed by taxpayer. 12-30-42 Granted to 2-8-43.

1943

Jan. 8—Hearing set Feb. 8, 1943, New York City.

Feb. 8—Hearing had before Judge Tyson on the merits. Submitted. Stipulation of facts filed at hearing. Briefs due as per Rules.

Feb. 19—Motion to amend stipulation of facts in part, embodying amendment, filed by General Counsel. 2-20-43 Granted.

Mar. 2—Transcript of hearing Feb. 8, 1943 filed.

Mar. 5—Brief filed by taxpayer.

Mar. 25—Brief filed by General Counsel. Served 3-26-43

[fol. 2] 1943

Mar. 26—Copy of brief served on General Counsel.

Apr. 9—Reply brief filed by taxpayer. 4-9-43 Copy served on General Counsel.

Oct. 8—Findings of fact and opinion rendered, Tyson, Judge, Div. 1. Decision will be entered for the petitioners. 10-8-43. Copy served.

Oct. 8—Decision entered, Tyson, Judge, Div. 1.

Dec. 28—Petition for review by U. S. Circuit Court of Appeals, 2nd Circuit, with assignments of error filed by General Counsel.

1944

Jan. 3—Proof of service filed by General Counsel. (2).

Jan. 22—Notice of the appearance of Geo. E. Cleary as counsel and S. Milton Simpson filed.

Jan. 22—Motion requesting leave to withdraw as counsel filed by A. Roberts MacMannis, filed.

Jan. 24—Motion requesting leave to withdraw as counsel filed by A. Roberts MacMannis, granted.

Feb. 24—Motion for extension to 4-26-44 to prepare and transmit the record filed by General Counsel.

Feb. 24—Order enlarging time to 4-26-44 to prepare and transmit the record entered.

Apr. 18—Motion for extension to 6-24-44 to prepare and transmit the record filed by General Counsel.

Apr. 18—Order enlarging time to 6-24-44 to prepare and transmit the record entered.

May 22—Praecipe for record filed with proof of service thereon.

[fol. 3] Before United States Board of Tax Appeals

Trust U/W of Mary Lily (Flagler) Bingham, Messrs. William R. Kenan, Jr., and Lawrence C. Haines, Trustees, petitioners,

v.

Commissioner of Internal Revenue, Respondent

Received Dec. 11, 1941. Chief Counsel's Office for the Bureau of Internal Revenue.

Received Dec. 11, 1941. U. S. Board of Tax Appeals.

Petition

The above named petitioners hereby petition for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency (Second New York Division, LAL-90D) dated September 19, 1941, and as a basis of their proceeding allege as follows:

1. The petitioners are fiduciaries with principal office at 120 Broadway, Room 1823, New York, New York. The petitioners' income tax return for the period here involved was filed with the Collector of Internal Revenue for the Second District of New York, Customhouse, New York, New York.

2. The notice of deficiency (a copy of which is attached and marked Exhibit "A") was mailed to the petitioners on September 19, 1941.

[fol. 4] 3. The taxes in controversy are income taxes for the calendar year *1940* and in the amount of *$160,815.10*.

4. The determination of tax set forth in the said notice of deficiency is based on the following error:

(*a*) The Commissioner of Internal Revenue erroneously held that the petitioners are not engaged in carrying on a trade or business within the meaning of Section 23 (a) of the Internal Revenue Code as amended, and are not entitled to expense deductions in the total amount of $210,741.93, on the erroneous theory that said expenses are not ordinary and necessary expenses incurred in carrying on a trade or business within the meaning of Section 23 (a) of the Internal Revenue Code as amended.

5. The facts upon which the petitioners rely as the basis for this proceeding are as follows:

(*a*) Mary Lily (Flagler) Bingham died July 27, 1917, leaving a last will and testament which was duly admitted to probate on August 3, 1917.

(*b*) During the calendar year 1940 and at the present time petitioners were the duly appointed and acting trustees under said will.

(*c*) Item Ninth of said will provides as follows:

> "All the rest and residue of my estate including all lapsed bequests or devises, shall be held for the

term of twenty-one years from the date of this will by my said Trustees in trust for the maintenance and administration and development of the Florida East Coast Railway and the Florida East Coast Hotel properties (which are hereinafter called 'principal properties') and the properties held by subsidiary Com-
[fol. 5] panies. And to that end, my said Trustees shall have power to sell any of my said residue estate, except the stocks and bonds of said 'principal properties,' to invest the proceeds of such sales and the income and increments of all my said residue estate in such securities or other properties as they may think best; to use any of the said proceeds or said income or increments for the benefit of any of said principal or subsidiary properties; to make and execute any and all obligations, and all pledges and mortgages of any of my said residue estate except the stocks and bonds of the said principal properties, which may be necessary for the purposes of the maintenance, administration or development of the said principal or subsidiary properties; to exchange any of said properties, other than the principal properties, and the stocks and bonds thereof, for any property which to them may seem desirable to be acquired for the benefit of the said principal or subsidiary properties, and continuingly to invest, sell and reinvest at such times and in such manner and in such sums and in such properties as may seem to them desirable for the purpose of carrying out the maintenance, administration and development of the said properties, the primary purpose of this trust being the keeping together of the enterprise into which my beloved husband, Henry M. Flagler, put so much of his energy, ambition and life."

(*d*) Item Fourteenth of said will provides as follows:

"Each of my said Trustees shall receive for his services as Trustee compensation at the rate of fifty thousand ($50,000.00) Dollars per year and such com-
[fol. 6] sation shall cover all services which he may render as Executor and be in full to him for all services in both capacities."

(*e*) During 1940, pursuant to the power conferred on them by Item Ninth and by Item Fourteenth of said will,

the petitioners paid out as ordinary and necessary expenses of carrying on the business of the trust estate, the following:

Compensation of Trustees		$141,369.86
Office Salaries		34,934.30
Office Supplies and Expenses		2,448.97
Petty Cash Expenditures		1,722.89
Office Rent	$11,700.32	
Less: Reimbursements	8,281.22	
		3,419.10
Legal Expenses		25,867.31
Tax and Financial Services		498.75
Micellaneous Expenses		480.75
Total		210,741.93

(*f*) Pursuant to the provisions of Item Fourteenth of said will, the petitioners paid on August 3, 1940, to William R. Kenan, Jr. $50,000.00 and on the same date to Lawrence C. Haines $50,000.00, a total of $100,000.00, as compensation in full for all services rendered for the period beginning August 3, 1939, and ended August 2, 1940.

(*g*) Pursuant to the provisions of Item Fourteenth of said will, the petitioners paid on December 20, 1940, to William R. Kenan, Jr. $20,684.93 and on the same date to Lawrence C. Haines $20,684.93, a total of $41,369.86, in full and FINAL compensation for all services rendered as Trustees of said trust estate for the period beginning Aug- [fol. 7] ust 3, 1940 and ended December 31, 1940, on which latter date distribution of the testamentary trust estate was concluded, except for some minor non-income producing properties, not here in issue.

(*h*) Pursuant to the provisions of Item Ninth of said will, the petitioners paid during the year 1940, in addition to the compensation of said Trustees at the rate provided in Item Fourteenth of said will, ordinary and necessary office salaries, office rent, and other office expenses, as set forth in paragraph (e) hereof, all in connection with the carrying on of the trade or business of the testamentary trust estate.

(*i*) During the calendar year 1940 the "subsidiary" companies referred to in Item Ninth of the last will and testa-

ment of Mary Lily (Flagler) Bingham were the following:

Florida East Coast Car Ferry Company,
West Palm Beach Water Company,
Model Land Company,
Perrine Grant Land Company,
The Record Company,
St. Augustine Golf Development Company,
Chuluota Company,

which said "subsidiary" companies were in addition to the "principal properties" referred to in Item Ninth of said will, as follows:

Florida East Coast Railway Company,
Florida East Coast Hotel Company.

(j) During the calendar year 1940 the petitioners were engaged in carrying on the trade or business of the trust estate which trade or business was separate and distinct from the trade or business carried on by the principal and [fol. 8] subsidiary companies set forth in paragraph (i) hereof.

Wherefore, the petitioners pray that this Board may hear the proceeding and determine that there is no deficiency in federal income tax liability of petitioners for the calendar year 1940.

William R. Kenan, Jr., Trustee; Lawrence C. Haines, Trustee, 120 Broadway, Room 1823, New York, New York.

Duly sworn to by William R. Kenan, Jr. and Lawrence C. Haines. Jurats omitted in printing.

[fol. 9] EXHIBIT "A" TO PETITION

Treasury Department

Internal Revenue Service

Office of Internal Revenue Agent in Charge, Second New York Division.

Sept. 19, 1941.

Trust U/W of Mary Lily (Flagler) Bingham, Messrs. William R. Kenan, Jr. and L. C. Haines, Trustees, Room 1823, 120 Broadway, New York, New York.

SIRS:

You are advised that the determination of your income tax liability for the taxable year(s) ended Dec. 31, 1940, [fol. 10] discloses a deficiency of $160,815.10 as shown in the statement attached.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency mentioned.

Within 90 days (not counting Sunday or a legal holiday in the District of Columbia as the 90th day) from the date of the mailing of this letter, you may file a petition with the United States Board of Tax Appeals for a redetermination of the deficiency.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to Revenue Agent in Charge, 12th Floor, 225 Broadway, New York, N. Y., for the attention of LAL-90D. The signing and filing of this form will expedite the closing of your return(s) by permitting an early assessment of the deficiency, and will prevent the accumulation of interest, since the interest period terminates 30 days after filing the form, or on the date assessment is made, whichever is earlier.

Respectfully, Guy T. Helvering, Commissioner, (Signed) by C. R. Krigbaum, Internal Revenue Agent in Charge.

Enclosures: Statement. Form of waiver.

[fol. 11] Statement

Trust u/w of Mary Lily (Flagler) Bingham, Messrs. William R. Kenan, Jr., and L. C. Haines, Trustees, Room 1823, 120 Broadway, New York, New York

Tax Liability for Taxable Year Ended December 31, 1940

	Liability	Assessed	Deficiency
Income tax	$473,444.37	$312,629.27	$160,815.10

In making this determination of your income tax liability, careful consideration has been given to the report of examination dated May 29, 1941; to your protest dated July 22, 1941; and to the statements made at the conferences held on August 19, August 28, and September 2, 1941.

Adjustment to Net Income

Net income as disclosed by return		$477,772.02
Unallowable deduction and additional income:		
(*a*) Other deductions		210,741.93
Net income adjusted		688,531.95

Explanation of Adjustment

(*a*) It is held that the following items claimed as deductions on line 13 of your return in the amount of $210,741.93 (part of a total of $261,741.93) are not ordinary and necessary expenses incurred in carrying on a trade or business within the meaning of section 23 (a) of the Internal Reve- [fol. 12] nue Code as amended. Accordingly, the deductions have been disallowed.

Compensation of trustees		$141,369.86
Office salaries		34,934.30
Office supplies and expenses		2,448.97
Petty cash		1,722.89
Office rent	$11,700.32	
Less: credit	8,281.22	
		3,419.10
Tax and financial services		498.75
Legal expenses		25,867.31
Miscellaneous		480.75
Total		210,741.93

Trust u/w of Mary Lily (Flagler) Bingham

Statement

Computation of Tax, Internal Revenue Code as Amended	
Net income adjusted	$688,513.95
Minus: Net long-term capital gain	1,293.75
Ordinary net income	687,220.20
Less: Personal exemption	100.00
Balance (surtax net income)	687,120.20
Net income subject to normal tax	687,120.20
Normal tax at 4% on $687,120.20	27,484.81
Surtax on $687,120.20	423,764.14
Partial tax	451,248.95
Plus: 30% of net long-term capital gain of $1,293.75	388.13
Alternative tax	451,637.08
Less: Income tax paid at the source	1,880.40
Correct income tax liability	449,756.68
Defense tax—10%	23,687.69
Total income and defense taxes due	473,444.37
Total income and defense taxes paid:	
Original, Account No. 187022	312,629.27
Deficiency of income tax	160,815.10

[fol. 13] BEFORE UNITED STATES BOARD OF TAX APPEALS

[Title omitted]

ANSWER

Comes now the Commissioner of Internal Revenue, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, and in answer to the petition filed herein, admits and denies as follows:

1. Admits the allegations contained in paragraph 1 of the petition.

2. Admits the allegations contained in paragraph 2 of the petition.

3. Denies the allegations contained in paragraph 3 of the petition, except it is admitted that the taxes in controversy are income taxes for the calendar year 1940.

4. Denies the Commissioner committed error as alleged in paragraph 4 (a) of the petition, and each and every allegation of fact contained therein.

5. Denies the allegations contained in paragraph 5 (a) to (j) inclusive, of the petition.

Denies generally and specifically each and every allegation contained in the petition not hereinbefore admitted, qualified or denied.

[fol. 14] Wherefore, it is prayed that the appeal be denied and the taxes as shown in the deficiency notice be in all respects approved.

J. P. Wenchel, H. D. T., J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue.

Of Counsel: E. C. Algire, Division Counsel; Thos. H. Lewis, Jr., Special Attorney, Bureau of Internal Revenue. lmv 12/26/41.

IN THE TAX COURT OF THE UNITED STATES

[Title omitted]

The Tax Court of the U. S. Filed at Hearing Feb. 8, 1943. New York. Division 1. Docket 109384.

STIPULATION OF FACTS

It is hereby stipulated and agreed by and between the parties hereto, by their respective counsel, that the facts hereinafter set forth shall be taken as true, provided, how-
[fol. 15] ever, that this stipulation shall be without prejudice to the rights of either party to introduce other and further evidence not inconsistent with or contradictory of the facts herein stipulated to be taken as true.

1. Mary Lily (Flagler) Bingham died on July 27, 1917. Attached hereto and made a part hereof, marked "Exhibit A", is a true copy of her Last Will and Testament.

2. At all times since prior to January 1, 1940, the petitioners in this proceeding, William R. Kenan, Jr. and Lawrence C. Haines, were the duly qualified and acting Trustees under the Will of said Mary Lily (Flagler) Bingham. Said petitioners filed an income tax return on Form 1041 (For Estates and Trusts) for the calendar year 1940 with the Collector of Internal Revenue for the Second District of New York, showing a Federal income and defense tax due of $312,629.27, which was duly assessed and paid.

3. The respondent determined a deficiency in petitioners' Federal income and defense tax for the calendar year 1940 in the amount of $160,815.10. A true copy of the notice of deficiency, dated September 19, 1941, is attached to the petition herein as "Exhibit A" thereof.

4. During the calendar year 1940, pursuant to the powers conferred on them by Item Ninth and by Item Fourteenth of said will, the petitioners paid out a total of $210,741.93, in connection with the carrying on of the provisions of the [fol. 16] Last Will and Testament of Mary Lily (Flagler) Bingham which created the Trust Estate:

Compensation of Trustees		$141,369.86
Office Salaries		34,934.39
Office Supplies and Expenses		2,448.97
Petty Cash Expenditures		1,722.89
Office Rent	$11,700.32	
Less: Reimbursements	8,281.22	
		3,419.10
Legal Fees and charges paid to Root, Clark, Buckner & Ballantine, attorneys-at-law, as hereinafter itemized		25,867.31
Tax and Financial Services		498.75
Miscellaneous Expenses		480.75
Total		210,741.93

5. The books and accounts of the petitioners have at all times been kept on the basis of cash receipts and cash disbursements, and the Federal income tax return for the calendar year 1940 (as well as in all prior years) was filed on the same basis as that upon which the books and accounts were kept, viz., cash receipts and cash disbursements.

6. Of the items disallowed in the said deficiency notice, (Exhibit "A" of the petition) the following are ordinary

and necessary expenses paid during the taxable year for the production or collection of income or for the management, conservation or maintenance of property held for the production of income:

Compensation of Trustees	$141,369.86
Office Salaries	34,934.30
Office Supplies and Expenses	2,448.97
Petty Cash Expenditures	1,722.89
Office Rent (net)	3,419.10
Tax and Financial Services	498.75
Miscellaneous Expenses	480.75
Total	184,874.62

[fol. 17] 7. During the calendar year 1940 the petitioners paid to Root, Clark, Buckner & Ballantine, attorneys-at-law, for legal fees and charges a total of $25,867.31, as follows:

	Fees	Expenses
Jan. 10 For services from August 27, 1937 to January 2, 1940 in contesting asserted deficiency in federal income tax for 1935 of $365,687.12 and expenses for stenographers, postage, telephone and telegraph, etc. (For particulars of this litigation see 40 B. T. A. 823)	$7,500.00	$259.21
Mar. 22 Stenographic services		228.75
Board of Tax Appeals—fee for filing appeal record		6.65
United States Circuit Court of Appeals—fee for filing transcript of record (For particulars of this litigation see 40 B. T. A. 823)		6.50
May 15 Stenographic services, postage, telephone tolls, etc., in connection with 1935 income tax deficiency. (For particulars of this litigation see 40 B. T. A. 823)		130.98
May 22 For services in connection with the payment of legacy to the University of North Carolina, under Item Eighth of Mrs. Bingham's Will	750.00	

		Fees	Expenses
	Stenographic services		30.85
July 11	Cost of printing transcript of record and briefs on appeal		407.92
	Stenographic services		162.05
	Telephone, postage, filing fees, etc. (For particulars of this litigation see 40 B. T. A. 823)		63.15
Sept. 23	Stenographic services, filing fees, telephone tolls, postage, etc., in connection with 1935 income tax deficiency, and termination of trust. (For particulars of this litigation see 40 B. T. A. 824)		160.17
[fol. 18]			
Dec. 6	Stenographic services in connection with termination of the trust		38.40
Dec. 13	For services in connection with the appeal on the federal income tax deficiency of $365,687.12 for the year 1935. (For particulars of this litigation see 114 F. (2d) 217)	7,500.00	14.58
Dec. 30	For services in considering the tax problems resulting from the expiration of the trust, advice as to the present status of the Trust for tax purposes, and as to various methods whereby the various properties of the Trust might be continued as a single unit in the future; investigation of various questions of law and preparation for the Trustees of a memorandum in which the recommendation was made that the stocks of certain companies owned by the Trust be placed in one or more Voting Trusts; formation of Voting Trusts; advice relative to indebtedness owed by two of the principal corpora-		

	Fees	Expenses
tions; preparation of documents; and assisting the Trustees in delivery of the assets of the Trust to the legatees	8,500.00	
Stenographic services and telephone tolls		108.10
Totals	$24,250.00	$1,617.31
	1,617.31	
Grand Total	$25,867.31	

Dated January 1943.

J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue. A. Roberts MacMannis, Counsel for Petitioners.

[fol. 19] EXHIBIT "A" TO STIPULATION OF FACTS

I, Mary Lily Flagler, do make, declare and publish this my last will and testament hereby revoking all former wills and testaments made by me:

Item First

I direct that all my debts, funeral expenses and the expenses of carrying out and administering the provisions of this instrument shall be fully paid.

Item Second

I hereby appoint Wm. R. Kenan, Jr., of the City of Lockport, in the State of New York, and Wm. A. Blount, of the City of Pensacola in the State of Florida, as the executors of and trustees under this my last will and testament, and I do hereby exempt them and each of them from the giving of any bond which may be required under any law or by any Court, and also exempt them from the filing of any inventories or accounts of my estate or of the administration thereof; and from the provisions of any law prescribing or restricting the character of property or securities in which they may invest the principal or income or other increments of my estate, as hereinafter provided.

Item Third

I give and devise unto my beloved niece, Louise Clisby Wise, if she shall survive me, all the real estate, wherever situated, which is now owned by me excluding from this [fol. 20] devise any real estate the title to which is vested in the Trustees under the will of my late husband Henry M. Flagler. While the absolute title and power of disposition will be in my said niece, it is my wish that if she does not dispose of the said property during her lifetime she shall dispose of it by will by which her father and any wife or children of him shall be excluded from any interest therein or use thereof.

Item Fourth

I give and bequeath to my said niece all my pearls, and to my brother's wife, Alice, one piece of jewelry, to be selected by my said Trustees, and to my sisters, Jessie Kenan Wise and Sarah Graham Kenan, all the rest of my jewelry share and share alike to be divided between them by my said Trustees, and their division to be final.

Item Fifth

All the rest and residue of the property, real and personal, of which I shall die seized and possessed, I give, devise and bequeath unto the said Wm. R. Kenan, Jr., and Wm. A. Blount, and their successors and assigns. In trust, however, as follows:

1. I give and bequeath unto and my Trustees shall deliver upon my death to my brother Wm. R. Kenan, Jr., my sister, Sarah Graham Kenan and my sister, Jessie Kenan Wise share and share alike the following oil stocks now owned by me to-wit:

Six thousand and fifty (6050) shares California Standard Oil Company stock;
[fol. 21] Forty-eight hundred (4800) shares Indiana Standard Oil Company stock;
Three Hundred (300) shares Kansas Standard Oil Company stock;
Four hundred and fifty (450) shares Kentucky Standard Oil Company stock;
One hundred and Fifty (150) shares Nebraska Standard Oil Company stock;

Sixteen Thousand (16000) shares New Jersey Standard Oil Company stock;

Twelve Thousand (12000) shares New York Standard Oil Company stock;

Five Hundred (500) shares Ohio Standard Oil Company stock.

If at the time of my death the said stocks shall be of less market value than their par values, my Trustees shall in addition to turning over to each of the said legatees one-third of said stocks, pay to each of them in cash the difference between the said par value and the said market value.

If any of the said stocks shall be sold by me before my death, the legacies herein given shall not fail as to said stocks so sold, but my Trustees shall upon my death pay to the said legatees share and share alike, the principal sum or sums for which I shall have sold the said stocks.

If my said brother or my sister, Jessie Kenan Wise, shall die before my death, the legacy to him or her herein provided for shall fail. But if my brother shall die before me, leaving a wife living at my death my Trustees shall pay to [fol. 22] her one-half Million ($500,000.00) Dollars and if my said sister, shall die before me, leaving a husband living at my death my Trustees shall pay to the said husband surviving one-half Million ($500,000,00) Dollars.

If my said sister, Sarah Graham Kenan shall die before me, leaving at my death no children the legacy to her herein provided for shall fail. But if she shall die before me leaving a husband, but no children living at my death my Trustees shall pay to him One-half Million ($500,000.00) Dollars. If however, my said sister shall die leaving living at my death a child or children or a child or children and a husband, then the legacy to my said sister herein provided for shall go to the said child, if there be but one, and there be no husband, or to the children share and share alike, if there be more than one and no husband, or to the husband and the child or children if there be a husband share and share alike.

2. I give to each of the following persons and my Trustees shall pay to them the following sums of money to-wit:

a. To my cousin Owen Kenan Three Hundred Thousand ($300,000.00) Dollars with deep affection from me.

b. To my faithful pastor and friend Dr. George Morgan Ward, twenty-five thousand ($25,000.00) Dollars.

c. To my cousin Emily Kenan, Twenty thousand ($20,000.00) Dollars.

d. To my cousin Thomas S. Kenan, Twenty thousand ($20,000.00) Dollars.

[fol. 23] *e.* To my Godchild, Mary Pope, daughter of John Russell Pope, of New York Twenty thousand ($20,000.00) Dollars.

f. To Mrs. Janet Mitchell (widow) of Raleigh, North Carolina, Twenty thousand ($20,000.00) Dollars.

g. To Mrs. J. B. McClellan, daughter of Mrs. Berry York of Cleveland, Ohio, Two thousand ($2,000.00) Dollars to be used by her for the purchase for her personal use of some thing in remembrance of me.

h. To W. H. Beardsley, Twenty-five thousand ($25,000.00) Dollars in appreciation for all his kindness to me.

i. To my faithful servant, Mary Monk, of Raleigh, North Carolina, Four thousand ($4,000.00) Dollars.

j. With deep affection to my faithful servant, Ida Remley Ten Thousand ($10,000.00) Dollars.

k. To Mary — (my cook) five thousand ($5,000.00) Dollars.

l. To George Holland, Five Thousand ($5,000.00) Dollars.

m. To James Weeks, Ten Thousand ($10,000.00) Dollars.

n. To Mollie Dick, wife of W. A. Dick, of Wilmington, North Carolina Ten Thousand ($10,000.00) Dollars.

o. To Mrs. Sue Corprew, wife of Burruss Corprew, of Norfolk, Virginia, Five Thousand ($5,000.00) Dollars.

p. To my Godchild John Lucas, son of Eugene Van Court Lucas, of Sound Beach, Connecticut, Five Thousand ($5,000.00) Dollars.

[fol. 24] *q.* To such persons as were Managers of the Ponce de Leon, Alcazar Ormond Beach, Royal Poinciana, The Breakers, Royal Palm and Colonial Hotels, at the time of the death of my husband, Henry M. Flagler, and who shall also be Managers of said Hotel at my death, Ten thousand ($10,000.00) Dollars each.

r. To the Trustees of the Memorial Presbyterian Church Society of Saint Augustine, Florida, Ten thousand ($10,000.00) Dollars.

s. To the Flagler Hospital at Saint Augustine, or to such Trustees, or other body representing it as may be entitled to receive the same, Ten Thousand ($10,000.00) Dollars.

t. To The Presbyterian Church, at Miami, Florida, or to such Trustees or other body representing it as may be entitled to receive the same, Ten Thousand ($10,000.00) Dollars.

u. To Miss Hannah P. Bolles of Wilmington, North Carolina, Ten Thousand ($10,000.00) Dollars.

v. To each of my servants who shall at the time of my death have been with me for the five immediately preceding consecutive years, One Thousand ($1,000.00) Dollars.

w. If any person to whom a legacy is given by this paragraph (Item Fifth, Paragraph 2) shall die before me, leaving a husband or wife, or child or children, living at my death such husband or wife or child or children, shall take the legacy herein given to the husband or wife or parent, as the case may be. And if the person so dead shall leave two or more of the said representatives, they shall take the legacy share and share alike.

[fol. 25] Item Sixth

I direct that each of the foregoing legacies given by paragraphs 1 and 2 of Item Fifth of this will shall be paid by my said Trustees as soon as in their judgment is compatible with the due administration of my estate and with the carrying out of my wishes with reference to the Florida East Coast Railway Company and the Florida East Coast Hotel properties hereinafter mentioned. Each of said money legacies shall bear interest from the time of my death until the time of its payment at the rate of four per cent per annum.

Item Seventh

That my said Trustees shall pay to my said niece, Louise Clisby Wise, the sum of Two Hundred Thousand ($200,000.00) Dollars annually until she shall have arrived at the age of forty (40) years at which time or as soon thereafter as compatible with the interests of my estate, they shall pay to her the sum of Five Million ($5,000,000.00) Dollars. If she shall die unmarried before my death or after my death and before she shall be forty years of age, this legacy shall fail but if she shall, before my death die married leaving living at my death a husband or child or children or after my death and before she shall be forty years of age, die married, leaving a husband and child or children the foregoing legacy shall go to them in equal shares, pay-

able at my death, if she die before me or upon her death, if she die after me, or in either case, as soon as compatible with the interests of my estate. But if she shall before my [fol. 26] death, die married, leaving only a husband living at my death, or die married after my death and before she shall be forty years of age, leaving only a husband living he shall receive from my Trustees, upon my death, if she die before me, or upon her death, if she die thereafter and before she shall be forty years of age, or in either case, as soon thereafter as compatible with the interests of my estate, the sum of One Million ($1,000,000.00) Dollars. The compatibility in every event above shall be determined absolutely by my Trustees.

Item Eighth

I give and bequeath and direct my Trustees to pay annually to the University of North Carolina, or such Trustees or other body representing it as may be entitled to receive the same, seventy-five thousand ($75,000.00) Dollars such sum however to be paid and received upon the trust that it shall be perpetually used by said University for the purpose of paying the salaries of professors thereof upon the condition that each of the professorships the salary of which is thus paid, shall be known as a Kenan Professorship this bequest being given in the interest of education of the youth of North Carolina, and also in memoriam of my father, Wm. R. Kenan, and my uncles, Thomas S. Kenan and James Graham Kenan, graduates of the said University. The said annual sum is to be paid during the continuance of the trust of my said Trustees and at the end of the said trust the said Trustees are to pay to the said University such sum in cash as at the rate of interest then [fol. 27] current in North Carolina will produce an annual income of seventy-five thousand ($75,000.00) Dollars, the amount of such sum to be determined by my said Trustees.

The Trustees may at their discretion if they think it compatible with the interests of my estate and the purpose of the trustee hereby created in them pay the said sum at any time prior to the expiration of the trust.

Item Ninth

All the rest and residue of my estate including all lapsed bequests or devises, shall be held for the term of twenty-

one years from the date of this will by my said Trustees in trust for the maintenance and administration and development of the Florida East Coast Railway and the Florida East Coast Hotel properties (which are hereinafter called "Principal properties") and the properties held by subsidiary Companies. And to that end, my said Trustees shall have power to sell any of my said residue estate, except the stocks and bonds of said "principal properties," to invest the proceeds of such sales and the income and increments of all my said residue estate in such securities or other properties as they may think best; to use any of the said proceeds or said income or increments for the benefit of any of said principal or subsidiary properties; to make and execute any and all obligations, and all pledges and mortgages of any of my said residue estate except the stocks and bonds of the said principal properties, which may be necessary for the purposes of the maintenance, administration or development of the said princi- [fol. 28] pal or subsidiary properties; to exchange any of said properties, other than the principal properties and the stocks and bonds thereof, for any property which to them may seem desirable to be acquired for the benefit of the said principal or subsidiary properties, and continuingly to invest, sell and reinvest at such times and in such manner and in such sums and in such properties as may seem to them desirable for the purpose of carrying out the maintenance, administration and development of the said properties the primary purpose of this trust being the keeping together of the enterprise into which my beloved husband, Henry M. Flagler, put so much of his energy, ambition and life.

Item Tenth

At the end of the said twenty-one years, the said Trustees shall divide the property then in their hands into three (3) equal parts, and shall execute such instruments, conveyances and transfers as may be necessary to vest one of said parts in each my brother, Wm. R. Kenan, Jr., my sister Mrs. Jessie Kenan Wise, and my sister Mrs. Sarah Graham Kenan and upon such transfers, conveyances and assignments the said trust shall cease. The judgment of the said Trustees as to the equality of the said parts shall be final.

If at the said time my brother Wm. R. Kenan, Jr., shall be dead, the legacy to him herein provided for shall fail; but if his wife shall be living, my Trustees shall pay to her the sum of Five Million ($5,000,000.00) Dollars. If he and [fol. 29] she shall both be dead, then the share which would have gone to him and to her under this item of my will, shall go to my sisters aforenamed, if they be then alive, share and share alike, or, if there be only one alive, then to the survivor.

If at the said time my sister Sarah Graham Kenan shall be dead, leaving no children the legacy to her herein provided for shall fail. But if she shall die before said time leaving a husband, but no children living at said time, my Trustees shall pay to him Five Million ($5,000,000.00) Dollars.

If, however, my said sister shall die leaving living at said time a child or children or a child or children and a husbond, then the legacy to her herein provided for shall go to the said child, if there be one, and there be no husband or to the children, share and share alike, if there be more than one, and no husband, or to the husband and to the child or children if there be a husband, share and share alike.

If my sister, Jessie Kenan Wise, at the said time, shall be dead this legacy to her herein provided for shall fail; but if she shall leave a husband living at said time my Trustees shall pay to him the sum of Five Million ($5,000,000.00) Dollars. If she shall be dead, leaving no husband, then the share which would have gone to her under this item of my will shall go to my brother and other sister aforenamed, if they be then alive, share and share alike, or, if there be only one alive, then to the survivor.

If all of the said brother and sisters shall die before the expiration of the said trust and my sister, Sarah Graham Kenan shall have no child or children and the aforesaid [fol. 30] Louise Clisby Wise shall be then living all of the property provided to go to my said brother and sisters by this paragraph shall go to the said Louise Clisby Wise. This provision however, shall not affect the provision hereinbefore made for the wife of my brother and the husband or husbands of my sister or sisters.

If the said Louise Clisby Wise shall die before the expiration of the said trust all the said residue estate shall

go to my heirs and distributees as determined by the now existing Law of Florida.

While the absolute title and power of disposition will be in my said niece, in the event that the said property shall vest in her, it is my wish that if she does not dispose of the said property during her life time she shall dispose of it by will in which her father, and any wife or children of him shall be excluded from any interest therein or use thereof.

Item Eleventh

My Trustees shall have the right to sell any of the property vested in them by this will (except the stocks and bonds of the principal properties) for the purpose, if necessary of paying any sum of money required to be paid by this will. They shall have the right, in the case of any such payment (except of the legacies given in Item Fifth, Paragraph 2) to substitute for the payment in money, payment in marketable securities of a value equal to the sum to be paid, the selection of the securities to be substituted in any instance, and the valuation of such securities to be done [fol. 31] by the Trustees and their selection and valuation to be final.

Item Twelfth

If any one of the said Trustees and Executors hereinunder shall at the time of my death not be living, or shall refuse or be unable to serve the remaining Trustee qualified and acting shall with the approval of the Circuit Judge of the Circuit embracing St. Johns County, Florida, fill the vacancy. If both be dead, or refuse or be unable to serve the said Judge shall fill the vacancies. Any vacancy or vacancies at any time thereafter occurring shall be filled in like manner. Each Trustee shall by virtue of his office as Trustee be also Executor of this will. Every substituted Trustee and Executor shall have all the title and exercise all the powers and have imposed upon him all the duties herein given to or imposed upon each of the Trustees and Executors herein named.

Item Thirteenth

I do further direct, ordain and declare and it is my will that if any person named in this instrument as a beneficiary or legatee, or devisee or any one interested there-

under shall at any time or in any manner institute, or cause to be instituted, or shall aid, abet, connive at or directly or indirectly promote the institution of any contest of proceeding or litigation contesting or intending to contest, defeat or obstruct, this instrument or any provision thereof, or the enforcement of any such provision then any and every such offending person or persons whether nat- [fol. 32] ural or artificial shall whether such contest proceeding or litigation be successful or not, thereby forfeit all interest under this instrument and the provision made in and by such instrument for any such offending person shall be of no effect and this instrument shall be executed and carried into effect as if such person were not therein named and no provision had been made therein as to or for such person.

Item Fourteenth

Each of my said Trustees shall receive for his services as Trustee compensation at the rate of fifty thousand ($50,000.00) Dollars per year and such compensation shall cover all services which he may render as Executor and be in full to him for all services in both capacities.

In witness whereof, I have hereunto and to each of the preceding typewritten twelve (12) pages which together with this typewritten page constitute my will set my hand and seal at White Sulphur Springs, in the County of Greenbrier and State of West Virginia, this 23d day of September, A. D. 1916.

Mary Lily Flagler. (Seal.)

Signed and sealed by the said Mary Lily Flagler in our presence and in the presence of each of us who in her presence and in the presence of each other and at her request sign our names hereto as witnesses.

J. Howard Slocum, Owen J. McLaughlin, S. B. Capito.

[fol. 33] State of Florida,
County of Palm Beach.

Be it remembered that on this 3rd day of August, A. D. 1917, I have duly recorded the foregoing will in the public records of said County.

Jerome E. Wideman, County Judge. (Seal.)

I, Mary Lily Bingham, wife of Robert W. Bingham of Louisville, Kentucky, being advised that my marriage to

him may have revoked a last will and testament made by me on the 23rd day of September, A. D. 1916, do hereby republish, re-affirm, adopt and declare the aforesaid instrument as my present will and testament in like manner as if the said will and testament were now executed by me.

In witness whereof, I have hereunto set my hand and seal this 8th day of December, A. D. 1916.

Mary Lily Bingham. (Seal.)

Signed and sealed by Mary Lily Bingham in our presence and in the presence of each of us, who at her request and in her presence and in the presence of each other hereunto sign our names as witnesses;

Stanley E. Slóss, of Louisville, Ky.; Emanuel Levi, of Louisville, Ky.; Emily A. Overman, of Louisville, Ky.

I, Robert W. Bingham, husband of Mary Lily Bingham, having been made acquainted with the contents of the will and testament above mentioned, made on the 23rd day of September (A. D. 1916, do hereby signify my assent to the re-publication, adoption, re-affirmation and re-declaration by my said wife of the said will.

In witness whereof, I have hereunto set my hand and seal this 8th day of December, A. D. 1916.

Robert W. Bingham. (Seal.)

[fol. 34] Signed, sealed and delivered in the presence of: Stanley E. Sloss, Emanuel Levi, Emily A. Overman.

STATE OF FLORIDA,
County of Palm Beach.

Be it remembered that on this 3d day of August, A. D. 1917, I have duly recorded the foregoing republication of will in the public records of said County.

Jerome E. Wideman, County Judge. (Seal.)

Palm Beach, Florida

March —, 1917.

I, Mary Lily Bingham, do hereby as a Codicil to my last will and testament, which I have heretofore made as Mary Lily Flagler direct my executors and Trustees to pay to the

Trustees or other governing body of the Flagler Hospital at Saint Augustine, Florida, a sum towards the construction and furnishing of said Hospital, not exceeding the sum of One hundred and twenty-five thousand dollars ($125,000.00) less such sums as may have been advanced by me or by my direction for said purposes prior to my death.

Mary Lily Bingham.

Signed, sealed and delivered by Mary Lily Bingham in the presence of her and of each of us, who at her request hereto sign our names as witnesses.

Owen Kenan, Sydney Capon.

[fol. 35] STATE OF FLORIDA,
County of Palm Beach.

Be it remembered that on this 3rd day of August, A. D. 1917, I have duly recorded the foregoing Codicil in the public records of said County.

Jerome E. Wideman, County Judge. (Seal.)

Dr. M. L. Ravitch

Louisville, Ky., June 19, 1917.

I make this a codicil to my last will and it shall be a valid devise as such codicil and if at my death I have no will or have a will or wills made subsequently to this instrument it shall nevertheless be an independent devise at all times and under all circumstances of change, modification or revocation of my present will or any will or wills. I give and bequeath to my husband, R. W. Bingham, five million ($5,000,000) Dollars to be absolutely his, and he shall have the option at my death of taking this from my estate in money or in such securities as he and the administering authorities of my estate may agree upon with respect to market values.

Witness my hand on the date above shown.

Mary Lily Bingham.

Witnesses, W. W. Davies, M. L. Ravitch.

Samuel W. Greene, Judge.

[fol. 36] IN THE TAX COURT OF THE UNITED STATES

TRUST U/W OF MARY LILY (FLAGLER) BINGHAM, MESSRS. William R. Kenan, Jr., and Lawrence C. Haines, Trustees, Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Docket No. 109384. Promulgated October 8, 1943

Under the facts, certain legal and miscellaneous expenses paid by petitioners *held* to be deductible from gross income as "non-trade or non-business expenses" under section 23(a) of the Internal Revenue Code as added by section 121 of the Revenue Act of 1942.

A. Roberts MacMannis, C. P. A., for the petitioners.
Thos. H. Lewis, Jr., Esq., for the respondent.

The respondent determined a deficiency in income tax against the petitioners for the calendar year 1940 in the amount of $160,815.10. The issue presented is whether the respondent erred in disallowing certain expense deductions taken by petitioners on their income tax return for that year.

The proceeding has been submitted upon the pleadings and a stipulation of facts. The stipulated facts not set forth are included herein by reference, except as hereinafter noted in the opinion.

FINDINGS OF FACT

At all times since prior to January 1, 1940, the petitioners were the duly qualified and acting trustees of a trust created by the will of Mary Lily (Flagler) Bingham, herein- [fol. 37] after mentioned. Their principal office was in New York, New York. They filed their income tax return for the taxable year with the collector of internal revenue for the second district of New York. Their books and accounts have always been kept on a cash basis and the income tax return filed by them for the taxable year was filed on the same basis.

Mary Lily (Flagler) Bingham died on July 27, 1917. By her will, which was dated September 23, 1916, and duly probated in August 1917, she appointed two in-

dividuals as executors and trustees and, after providing for a certain devise of real estate and certain specific bequests of jewelry, provided for the conveyance to the trustees of all the residue of the property, real and personal, of which she should die seized and possessed. The will provided for the payment by the trustees to various parties of at least $536,000 in cash legacies and for the delivery by the trustees to various other parties of 40,250 shares of Standard Oil Co. stock. All those beneficiaries were to receive their legacies as soon as compatible with the due administration of the estate and the carrying out of the testator's wishes with reference to the hotel and railroad properties mentioned in item ninth of the will hereinafter set out. The will further provided for the payment of $200,000 annually to a niece of the testator until that niece attained the age of 40 years, when she was to be paid the lump sum of $5,000,000, if compatible with the interest of the estate as determined by the trustees. The will also [fol. 38] provided that the trustee should pay $75,000 annually to the University of North Carolina during the continuance of the trust and at the expiration thereof should pay to the university such a sum in cash as would produce an annual income of $75,000.

Item ninth of the will provided as follows:

> All the rest and residue of my estate including all lapsed bequests or devises, shall be held for the term of twenty-one years from the date of this will by my said Trustees in trust for the maintenance and administration and development of the Florida East Coast Railway and the Florida East Coast Hotel properties (which are hereinafter called "Principal properties") and the properties held by subsidiary Companies. And to that end, my said Trustees shall have power to sell any of my said residue estate, except the stocks and bonds of said "principal properties," to invest the proceeds of such sales and the income and increments of all my said residue estate in such securities or other properties as they may think best; to use any of the said proceeds or said income or increments for the benefit of any of said principal or subsidiary properties; to make and execute any and all obligations, and

all pledges and mortgages of any of my said residue estate except the stocks and bonds of the said principal properties, which may be necessary for the purposes of the maintenance, administration or development of the said principal or subsidiary properties; to exchange any of said properties, other than the principal properties and the stocks and bonds thereof, for any property which to them may seem desirable to be acquired for the benefit of the said principal or subsidiary [fol. 39] properties, and continuingly to invest, sell and reinvest at such times and in such manner and in such sums and in such properties as may seem to them desirable for the purpose of carrying out the maintenance, administration and development of the said properties the primary purpose of this trust being the keeping together of the enterprise into which my beloved husband, Henry M. Flagler, put so much of his energy, ambition and life.

The will further provided that each of the trustees should receive compensation at the rate of $50,000 a year for services as trustee and such compensation also should cover all services which each trustee might render as executor.

At the end of 21 years from the date of the will the trustees were to divide the property then in their hands into three equal parts and transfer such parts to the testator's two sisters and brother in equal shares.

The respondent's determination of a deficiency resulted from the allowances of $210,741.93 expenses paid by petitioners in the taxable year and deducted by them from gross income in their income tax return for that year. The respondent's reason for the disallowance of these expenses was that they were not ordinary and necessary expenses incurred in carrying on a trade or business within the meaning of section 23 (a) of the Internal Revenue Code. By stipulation the parties have agreed that all of the expenses originally disallowed by the respondent were ordinary and necessary expenses paid during the taxable year for the production or collection of income or for the management, conservation, or maintenance of property held [fol. 40] for the production of income, save one item of

$25,867.31 paid for legal fees and charges. The expenses so agreed upon are as follows:

Compensation of trustees	$141,369.86
Office salaries	34,934.30
Office supplies and expenses	2,448.97
Petty cash expenditures	1,722.89
Office rent (net)	3,419.10
Tax and financial services	498.75
Miscellaneous expenses	480.75
Total	184,874.62

Of the legal fees and charges of $25,867.31 paid by the petitioners, $16,439.96 was incured for services rendered from August 1937 to January 1940 in contesting a deficiency of $365,687.12 in income tax asserted against the petitioners for the year 1935. This deficiency was asserted by reason of the inclusion by the Commissioner in income of alleged gains of $1,991,316.75 resulting from the partial payment in 1935 in securities of a bequest to Louise Clisby Wise of $5,000,000 under the above mentioned will. The payment was made under the provision of the will that when Louise Clisby Wise reached the age of forty, or as soon thereafter as was compatible with the interests of the estate, she was to be paid the sum of $5,000,000. When Louise Clisby Wise became forty years of age the trustees paid her $5,000,000, partly in cash and partly in securities. Some of the securities had been purchased by the trustees and some had been received by the trustees as part of the estate of the decedent at her death, which later securities had appreciated in value during the period held by the trustees, and the respondent determined that, to the extent [fol. 41] that the value of the securities purchased exceeded their cost and to the extent of the appreciation of the other securities, the distribution thereof resulted in capital gains taxable as specified in section 117 of the Revenue Act of 1934. In the case of *William R. Kanan, Jr., et al., Trustees*, 40 B. T. A. 824, we sustained the respondent's determination of the deficiency. Our decision sustaining the deficiency was appealed to the Circuit Court of Appeals for the Second Circuit. That Circuit Court, in *Kenan* v. *Commissioner*, affirmed our decision in 114 Fed. (2d) 217. The legal fees here in dispute were paid for services rendered

by attorneys in connection with the proceeding there before us and in connection with the appeal therefrom. Payments to the attorneys also covered reimbursements for expenses incurred by them in contesting the deficiency.

Of the legal fees and charges paid by the petitioners, the amount of $780.85 was for services in connection with the payment of the above mentioned legacy to the University of North Carolina and for stenographic expense incurred by the attorneys in connection with those services.

The remaining $8,646.50 of the total of $25,867.31 in legal fees and charges paid by the petitioners in 1940 was for services rendered in respect of the tax and other problems resulting from the expiration of the trust and delivery of its assets to the legatees.

OPINION

TYSON, *Judge*: The parties have stipulated that $184,874.62 of the expenses in question were ordinary and [fol. 42] necessary expenses paid during the taxable year for the production or collection of income or for the management, conservation, or maintenance of property held for the production of income, and respondent, on brief, concedes that such amount is deductible. We accordingly hold that those expenses are deductible from petitioners' gross income.

The question is then presented as to whether the other expenses of $25,867.31 are also deductible from petitioners' gross income.

Petitioners' first contention is that under item ninth of the will they, as trustees, were carrying on the business of the maintenance, administration, and development of the properties of the hotel, railway, and subsidiary companies, stocks and bonds of which companies were owned by them, the amount thereof and their proportions of the totals outstanding not being shown; that the expenses were incurred and paid in that business; and that those expenses are consequently deductible under section 23 (a) (1) of the Internal Revenue Code or that subsection as carried forward into section 121 of the Revenue Act of 1942. Petitioners make no argument that they were carrying on a business of any other character.

There is nothing in the record showing in what activities, if any, petitioners were engaged with reference to the

maintenance, administration, or development of the properties of the hotel, railway, and subsidiary companies, and there is also nothing in the record to show that the petitioners participated, directly or indirectly, in the manage-[fol. 43] ment of any of those companies or their properties. We are therefore unable to say that the trustees were engaged in the carrying on of the business of the maintenance, administration, or development of such properties, as contended by petitioners. In reaching this conclusion we have not overlooked that part of the stipulation of facts stating that the expenses were paid by the trustees "pursuant to the powers conferred on them by Item Ninth * * * of said will." The trustees were empowered by item ninth to sell, invest, and reinvest, and to use the income and increment, and to mortgage, pledge, and exchange properties, for the purpose of maintaining, administering, or developing the principal properties; but the amounts here in question, as shown by our findings and as itemized in the stipulation, clearly were not expended in the exercise of any of these powers. In this situation we are not bound by the conclusion contained in the part of the stipulation quoted above and that portion must be disregarded in determining whether the trustees were engaged in the carrying on of the business of the maintenance, administration, or development of the principal properties of the hotel, railway, and subsidiary companies, as contended by the petitioners. *Ernst Kern Co.*, 1 T. C. 249, 265; *William Ernest Seatree*, 25 B. T. A. 396; affd., 72 Fed. (2d) 67; *T. K. Harris Co.*, 38 B. T. A. 383; affd., 112 Fed. (2d) 76.

Assuming however that the trustees were engaged in carrying on the business of the maintenance, administration, [fol. 44] and development of the properties of the hotel, railway, and subsidiary companies, it is clear that none of the $25,867.31 expenses was incurred or paid for the purpose of the carrying on of that business. All of it was incurred and paid in connection with the payment of legacies and distributions from the estate by the trustees to the beneficiaries entitled thereto and the expiration of the trust, as is shown in our findings and the itemization of those expenses in the stipulation of facts.

We are of the opinion, and so hold, that the expenses of $25,867.31 were not expenses incurred and paid in carrying on a trade or business within the provision of section 23

(a) (1) of the Internal Revenue Code or of that subsection as carried forward into section 121 of the Revenue Act of 1942, as contended by petitioners.

Since the determination of the deficiency herein Congress has enacted section 121 of the Revenue Act of 1942, retroactively amending section 23 (a) of the Internal Revenue Code,[1] and that section as amended applies to the taxable [fol. 45] year here involved. Therefore, there remains the question of whether the expenses we are considering are deductible under that amendment. Section 121, *supra*, is applicable to the income of a trust such as the one here involved. (Secs. 161 and 162, Internal Revenue Code.)

Petitioners contend alternatively that, if the expenses were not incurred and paid in the carrying on of a business, they were paid and incurred as a "nontrade or nonbusiness expense" within that provision of section 23 (a) (2) of the Internal Revenue Code as added by section 121 (a) of the

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[1] SEC. 121. NON-TRADE OR NON-BUSINESS DEDUCTIONS.

(a) DEDUCTION FOR EXPENSES.—Section 23 (a) (relating to deduction for expenses) is amended to read as follows:

"(a) EXPENSES.—

"(1) TRADE OR BUSINESS EXPENSES.—

"(A) IN GENERAL.—All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered; traveling expenses (including the entire amount expended for meals and lodging) while away from home in the pursuit of a trade or business; and rentals or other payments required to be made as a condition to the continued use or possession, for purposes of the trade or business, of property to which the taxpayer has not taken or is not taking title or in which he has no equity.

. . . . . .

"(2) NON-TRADE OR NON-BUSINESS EXPENSES.—In the case of an individual, all the ordinary and necessary expenses paid or incurred during the taxable year for the production or collection of income, or for the management, conservation, or maintenance of property held for the production of income."

. . . . . .

Revenue Act of 1942, which allows deductions for expenses "paid or incurred * * * for the management, conservation or maintenance of property held for the production of income." They concede, on brief, that the expenses involved had no connection with the "production or collection of income" as those words are used in section 23 (a) (2). There is no dispute over whether the claimed deductions were ordinary and necessary expenses.

Respondent, on brief, concedes that the trust property was "held for the production of income" as those words are [fol. 46] used in section 23 (a) (2), *supra*, but contends that nevertheless the expenses involved were not incurred or paid for managing, conserving, or maintaining the property so held, because, he argues, the expenses were proximately caused, not by such holding of the property, but by its distribution, and states more particularly that the management of the property of a trust does not embrace any act pertaining to the distribution or "settling up" of the trust estate.

The litigation in 40 B. T. A. 824, and 114 Fed. (2d) 217, arose in connection with property held for the production of income which the petitioners were managing, and, while the expenses of that litigation were paid as a result of the payment by petitioners as trustees of a bequest of $5,000,000 to Louise Clisby Wise, the sole purpose and object of the litigation and the proximate cause of the expenditure were to relieve the estate from the payment of the deficiency in income tax determined by the Commissioner, which was the subject matter of the litigation. The effort of petitioners in seeking, through this litigation, to give such relief to the estate was, in our opinion, obviously a factor in the conservation, management, and maintenance of the property of that estate, concededly held for the production of income, since in resisting the imposition of the tax the trustees were performing the required duty of protecting and defending the trust property in their hands against any claim or lien for the tax. Even if, on the facts presented, it could fairly be said that the distribution of the $5,000,000 bequest was the proximate cause of the expenses paid in [fol. 47] connection with the litigation, those expenses would then be essentially of the same character as those other expenses which are immediately hereinafter considered and would be deductible as expenses paid for the "management" of the property for the same reasons.

We hold that the expenses of the litigation are deductible from petitioners' gross income under section 23 (a) (2) of the Internal Revenue Code as added by section 121 of the Revenue Act of 1942.

As to the balance of the controverted expenses, amounting to $9,427.35, we are of the opinion that they are also deductible from the gross income of petitioners under the same statute. The subject matter with regard to which those expenses were incurred and paid involved problems arising out of the payment of a bequest to the University of North Carolina, the expiration of the trust, and distribution of its assets to the legatees, and such payment and distribution were made by the trustees as directed by the will and as a part of their duties in managing the trust property.

That those expenses incidental and necessary to the payment of the University of North Carolina legacy and the "settling up" of the trust estate through distribution of its property held here by the trustees for the production of income are deductible under section 23 (a) (2) of the Internal Revenue Code as added by section 121 (a) of the Revenue Act of 1942 is, in our opinion, clear; since one, if not the most vital duty imposed upon those trustees was to make proper distribution of such property, and in making it they were performing one of the principal functions of the [fol. 48] management of such property, since until that property reached the hands of the legatees and distributees the trustees were in complete control of it, and thus its management. "Management" is the act of managing; the manner of treating, directing, carrying on, or using, for a purpose; conduct; administration; guidance; control. (Webster's New Int. Dict.) The expenses were incurred and paid prior to the distribution and while the property still remained in the hands and in the complete control of the trustees.

This is not a case where the expenses in question were paid in the course of the administration of the estate and where the expenses would be deductible from the gross estate for estate tax purposes rather than from gross income. In the first place the trust here was a long term trust to endure for 21 years from September 23, 1916, and that the expenses in question were not incurred or paid in the course of the administration of the estate is further demon-

strated by the facts that the first payment of a legacy (the one to Louise Clisby Wise) with respect to which the expenses of the suit above mentioned were incurred and paid was in 1935; that the payment of the other legacy, to the University of North Carolina, with respect to which other of these expenses were incurred and paid, was made at or about the time of the expiration of the trust; and that the balance of the expenses of $25,867.31 was incurred and paid in connection with and as a result of the expiration of the trust and delivery of its assets to the legatees.

We conclude that the expenses paid in connection with the payment of the legacy to the University of North Carolina, [fol. 49] the expiration of the trust, and the distribution of the assets of the trust estate were "for the management, * * * of property held for the production of income" and we hold that the amount so expended is deductible from gross income of petitioners within the purview of section 23 (a) (2) of the Internal Revenue Code as added by section 121 (a) of the Revenue Act of 1942.

Reviewed by the Court.

Decision will be entered for the petitioners.

CONCURRING OPINION

KERN, J., concurring:

I concur in the result reached by the majority opinion only because I conceive that the management of the property of the estate embraced the proper disposition of it pursuant to the will of the decedent, and that the expenses of litigation arising out of the disposition of the property of the estate are consequently "ordinary and necessary expenses paid * * * for the management * * * of property held for the production of income," and deductible under section 121, quoted in the majority opinion. The mere fact that the purpose of the expenditure was to relieve the estate from the payment of the deficiency in income tax and to protect the property of the estate from any tax lien, does not, in my opinion, characterize the expenditure as one paid or incurred "for the management, conservation, or maintenance of property held for the production of income." See *John W. Willmott*, 2 T. C. 321, 326, 327.

SMITH, J., agrees with the above.

DISSENTING OPINION

DISNEY, J., dissenting:

The majority opinion first holds deductible, only under [fol. 50] section 121 of the Revenue Act of 1942, the expenses of contesting a deficiency which was determined by the Commissioner on the theory that taxable gain was realized through the payment of a legacy in securities which had appreciated in value. The reason given for such allowance is that the effort of the petitioner through the litigation to give relief to the estate was a factor in the conservation, management, and maintenance of the property of the estate, since in resisting the imposition of the tax the trustees were performing their duty in defending the trust property against the claim for tax. I can not agree with that conclusion. The mere fact that the payment of the deficiency would consume resources of the estate is no sufficient answer for allowing the deduction, for on such a theory any expense of any litigation, incurred by a trust or an individual, would be deductible merely because the litigation might have terminated in a judgment collectible out of the property or estate of the litigant, and without regard to whether the litigation concerned property held for the production of income. For instance, on the same theory, expenses of defending litigation for personal injuries caused by negligence would be deductible, though having no connection with properties held for the production of income. Regulations 103, as amended in the light of section 142 of the Revenue Act of 1942, in my opinion properly provide that expenditures incurred for the purpose of resisting a proposed additional assessment of taxes are not deductible, unless the taxes are on property held for the production of [fol. 51] income. The tax involved in the deficiency which was litigated was not a tax upon the property held by the estate, but upon gain realized in the act of paying a legacy. Clearly, I think, paying the legacy can not be called conservation, management, or maintenance of the property of the estate, within the terms of the statute, for the property of the estate was being disposed of instead of being maintained, managed, or conserved. In my view, the words were used in their usual significance, intended to allow the ordinary and necessary expense requisite to the proper preservation or use of the property involved, such, for example, as repairs and expenses of supervision; but I do not believe

that the deduction may properly be allowed merely because, to use the words of the majority opinion, "in resisting the imposition of the tax the trustees were performing the required duty of protecting and defending the trust property in their hands against any claim or lien for the tax." This is not a question of the duty of the trustees under the trust instrument, but one as to whether ordinary and necessary expenses were paid "for the management, conservation, or maintenance of property" held for the production of income, and I can not subscribe to the idea that to litigate any question which might result in a judgment collectible out of that property is to manage, conserve, or maintain it, within the intendment of the statute. I therefore think that the expense of litigation over the deficiency does not come within the statute.

[fol. 52] Nor can I agree that the expenses for services in connection with the payment of the legacy to the University of North Carolina and "other problems resulting from the expiration of the trust and delivery of its assets to the legatees," as the majority opinion expresses the facts, are deductible under the statute. The majority opinion allows these also, on the theory that in distributing the property under the trust instrument the trustees were managing it. Apparently, conservation or maintenance of the property is not relied upon in the majority view. Again, however, I note that Regulations 103, amended to cover section 121 of the Revenue Act of 1942, provides, as to expenditures of executors or administrators, that expense incurred "in distributing the remaining assets to the beneficiaries or in conserving the assets for ultimate distribution to the parties entitled thereto are not deductible under this section." The same logic applies to distributions by trustees. I do not think that it was the intent of the statute to so broaden the meaning of the word "management" as to include expenses of distributing an estate. Not only is the statute providing for a deduction to be strictly construed, but also ordinary significance of the word must be assumed. I note that *In re Knight's Estate*, 208 N. Y. S. 822, involved trustees required by will to manage realty. It was held, "The word 'manage' implies the supervision, maintenance, and care of the premises, the making of necessary repairs, and the payment of taxes and water rents," and therefore that [fol. 53] these duties, not being upon the trustees after the property had been leased for a long period, the trustees

were not entitled to commissions upon the rents. We think the above quotation is a fair definition of "manage," with reference to the property of an estate and that the term does not connote such duties as distributing the property under a will or trust instrument. Indeed, the distribution and winding up of an estate or trust, through it may have to do with property included in the estate, is in a very real sense merely the performance of a legal function or duty under the will or trust instrument, not of the same character as the actual handling or dealing with the property itself. Distribution would be necessary, though only cash in hand was involved. Such performance of general administrative duty is, in my opinion, sufficiently distinct from the management or even the management, conservation, or maintenance of property in the usual and ordinary sense, as to require the conclusion that Congress did not intend to include it within the statutory expression. The statute does not provide for the expenses of management of an estate or trust, but "of property." To enlarge the meaning of the word, as is done by the majority opinion, is, as I see it, judicial legislation; and if such effect is desirable, I think the matter should be left to Congress. In my opinion, section 121 does not, as the majority opinion holds, cover the situation.

HARBON, J., agrees with this dissent.

[fol. 54] IN THE TAX COURT OF THE UNITED STATES

Washington

Docket No. 109384

TRUST U/W OF MARY LILY (FLAGLER) BINGHAM, MESSRS. William R. Kenan, Jr., and Lawrence C. Haines, Trustees, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Received in Docket Section Oct. 8, 1943, 4:09 P. M. Appeals Division Off. Chief Counsel, Bureau Internal Rev.

Received Oct. 1, 1943. Counsel, New York Division, New York City Office.

DECISION

Pursuant to the determination of the Court, as set forth in its Findings of Fact and Opinion, promulgated October 8, 1943, it is

Ordered and decided: That there is no deficiency in income tax for the calendar year 1940.

[Signed] John A. Tyson, Judge.

Entered Oct. 8, 1943.

[fol. 55] UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT, OCTOBER TERM, 1944

No. 90

(Argued October 12, 1944. Decided November 10, 1944)

COMMISSIONER OF INTERNAL REVENUE, Petitioner,

against

WILLIAM R. KENAN, JR., and LAWRENCE C. HAINES, as Trustees under the Will of Mary Lily (Flagler) Bingham, Respondents

Before L. Hand, Augustus N. Hand and Chase, Circuit Judges

Petition of the Commissioner of Internal Revenue to review an order of the Tax Court of the United States determining that there was no deficiency in federal income tax liability of the respondents William R. Kenan, Jr., and Lawrence C. Haines, as Trustees under the Will of Mary Lily (Flagler) Bingham for the calendar year 1940. Reversed.

[fol. 56] Samuel O. Clark, Jr., Assistant Attorney General, Sewall Key, J. Louis Monarch and L. W. Post, Special Assistants to the Attorney General, for the petitioner, Commissioner of Internal Revenue.

George E. Cleary, Attorney and counsel for respondents William R. Kenan, Jr., and Lawrence C. Haines, as Trustees under the Will of Mary Lily (Flagler) Bingham.

AUGUSTUS N. HAND, Circuit Judge:

The question before us is whether $25,867.31 paid in the year 1940 by the respondents as trustees under the will of Mary Lily (Flagler) Bingham were "ordinary and necessary expenses paid or incurred during the taxable year for the production or collection of income, or for the management, conservation, or maintenance of property held for the production of income" and thus deductible in computing their income tax under Section 23 (a) (2) of the Internal Revenue Act of 1942 which amended Section 23 (a) by adding subdivision (2) *supra*. The Tax Court allowed the de-

duction and the Commissioner of Internal Revenue appeals. In our opinion the Commissioner is right and the decision of the Tax Court must be reversed.

The $25,867.31 objected to by the Commissioner, but allowed by the Tax Court, were part of the sum of $210,741.93 paid by the trustees as expenses all of which were allowed by the Tax Court and all but the $25,867.31 were stipulated by the parties to have been "ordinary and necessary expenses paid during the tax year for the production or collection of income or for the management, conservation or mainatenance of property held for the production of income."

[fol. 57] The items constituting the $25,867.31 were all fees and charges paid to the attorneys for the trustees in the following amounts and relating to the following services:

(1) Items amounting to $16,439.96 represented fees and charges paid by the trustees to their attorneys in connection with the litigation as to income taxes before this court dealt with in our opinion reported in *Kenan Jr.* v. *Commissioner*, 114 F. (2d) 217. The question there decided against the trustees was whether a distribution by the trustees to a legatee in payment of $5,000,000 upon her reaching forty years of age resulted in a taxable gain to the trust where the securities distributed in payment had appreciated in value during the period during which they were held by the trustees. We there held that the appreciation was taxable as a capital gain.

(2) Items amounting to $780.85 represented fees and charges of the trustees' attorneys for services in connection with the annual payment of $75,000 by the trusees during the continuance of the trust to the University of North Carolina.

(3) The remaining items aggregating $8,646.50 consisted of fees and charges of the trustees' attorneys paid by the trustees for services in respect to the tax and other problems resulting from the expiration of the trust and delivery of the corpus to the legatees in remainder. The amount paid for fees included in (3) was for the following services as set forth in the stipulation of the parties:

> "For services in considering the tax problems resulting from the expiration of the trust, advice as to the present status of the

Trust for tax purposes, and as to various methods whereby the various properties of [fol. 58] the Trust might be continued as a single unit in the future; investigation of various questions of law and preparation for the Trustees of a memorandum in which the recommendation was made that the stocks of certain companies owned by the Trust be placed in one or more Voting Trusts; formation of Voting Trusts; advice relative to indebtednes owed by two of the principal corporations; preparation of documents; and assisting the Trustees in delivery of the assets of the Trust to the legatees ..... $8,500.00"

It is the contention of the Commissioner that all of the foregoing expenses were paid by the trustees in connection with the distribution of the property to legatees under the will of Mary Lily (Flagler) Bingham, were in the nature of capital expenditures and were not deductible under Section 23 (a) (2) of the Internal Revenue Act as amended. A majority of the Tax Court held that the above legal fees and charges were necessary expenses paid "for the management, conservation or maintenance of property held for the production of income" and, as such, were properly deductible.

The payment of $16,439.96 made by the trustees for legal services in connection with the litigation of *Kenan, Jr.* v. *Commissioner*, 114 F. (2d) 217, in which they had sought to establish that the appreciation in value of the securities turned over to the legatee as a part payment of the legacy of $5,000,000 bequeathed under the will of Mary Lily (Flagler) Bingham did not represent a "taxable" gain to the estate, cannot be regarded a payment for the "management, conservation or maintenance of property held for the production of income." It was not made as a recompense for management or maintenance of the trust property since that property was not held for the production of income but was [fol. 59] in the hands of the trustees ready for distribution. Taxes laid upon it had nothing to do with the production of taxable gain or ordinary income. The expense of contesting the taxes had no relation to the "management, conservation or maintenance of property held for the production of in-

come." The contest was not in order to produce income and the expenditure accordingly had no bearing upon such a purpose. To be deductible as expenses for management they must relate to the production of income or to the maintenance of property held for that purpose. They were not deductible when incurred merely to prevent the incidence of taxes which neither affected the yield of investment capital nor its appreciation.

In *Stoddard* v. *Commissioner*, 141 F. (2d) 76, we held that a payment to accountants for services in contesting income taxes assessed against an individual were not deductible under Section 23 (a) (2). Fees paid to lawyers for a similar object plainly are not different. The Court of Appeals of the First Circuit denied such a deduction in *Higgins* v. *Commissioner*, 143 F. (2d) 654, and the Court of Appeals of the Sixth Circuit in *Hord* v. *Commissioner*, 143 F. (2d) 73, rendered a decision to much the same effect. It does not seem reasonable to suppose that litigating the question whether a taxable gain in the trust securities had arisen was to manage or conserve or maintain the securities which had appreciated in value.

The items of $780.85 for services in connection with the annual payments to the University of North Carolina were not deductible as expenses. They had no relation to the production of income, or to the conservation of property held for that purpose. They only related to legal advice in respect to distribution to a legatee, and not to the management of any property held for the production of income. Only by an extremely liberal interpretation of an exemption clause, which must be construed not broadly but strictly, [fol. 60] could such services be regarded as coming within the meaning of the word "management."

The items aggregating $8,646.50 were likewise paid for services connected with the distribution of the trust estate and not with the production of income or the management of property held for the production of income. The services were performed after the trust had ended and only a distribution of the corpus to the legatees under the will remained to be effected. Advice in keeping the trust assets together and forming voting trusts for that purpose and work in setting up such voting trusts involved personal services rather than management of the trust estate by trustees. Any other payments for services which might possibly be thought to come within Section 23 (a) (2) are

not sufficiently disclosed in the record to justify regarding them as deductible for income tax purposes.

In view of the foregoing, the order of the Tax Court is reversed and the proceeding remanded.

[fol. 61] UNITED STATES CIRCUIT COURT OF APPEALS, SECOND CIRCUIT

At a Stated Term of the United States Circuit Court of Appeals, in and for the Second Circuit, held at the United States Courthouse in the City of New York, on the 27th day of November one thousand nine hundred and forty-four.

Present: Hon. Learned Hand, Hon. Augustus N. Hand, Hon. Harrie B. Chase, Circuit Judges.

COMMISSIONER OF INTERNAL REVENUE, Petitioner,

v.

TRUST U/W OF MARY LILY (FLAGLER) BINGHAM, et al., Trustees, etc., Respondents

Appeal from the Tax Court of the United States

This cause came on to be heard on the transcript of record from The Tax Court of the United States, and was argued by counsel.

On Consideration Whereof, it is now hereby ordered, adjudged, and decreed that the order of said The Tax Court of the United States be and it hereby is reversed and the proceeding remanded.

It is further ordered that a Mandate issue to the said The Tax Court of the United States in accordance with this decree.

Alexander M. Bell, Clerk.

[fol. 62] [Endorsed:] United States Circuit Court of Appeals, Second Circuit. Commissioner of Internal Revenue, v. Trust U/W of Mary Lily (Flagler) Bingham, et al., Trustees, etc. Order for Mandate. United States Circuit Court of Appeals, Second Circuit. Filed Nov. 27, 1944. Alexander M. Bell, Clerk.

[fol. 63] UNITED STATES OF AMERICA,
Southern District of New York:

I, Alexander M. Bell, Clerk of the United States Circuit Court of Appeals for the Second Circuit, do hereby certify that the foregoing pages, numbered from 1 to 62, inclusive, contain a true and complete transcript of the record and proceedings had in said Court, in the case of Commissioner of Internal Revenue, Petitioner, against Trust U/W of Mary Lily (Flagler) Bingham, Messrs. William R. Kenan, Jr., and Lawrence C. Haines, Trustees, Respondents, as the same remain of record and on file in my office.

In Testimony Whereof, I have caused the seal of the said Court to be hereunto affixed, at the City of New York, in the Southern District of New York, in the Second Circuit, this 18th day of January, in the year of our Lord one thousand nine hundred and forty-five, and of the Independence of the said United States the one hundred and sixty-ninth.

Alexander M. Bell, Clerk. (Seal.)

[fol. 64] SUPREME COURT OF THE UNITED STATES

ORDER ALLOWING CERTIORARI—Filed March 12, 1945

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Second Circuit is granted, and the case is transferred to the summary docket.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

Endorsed on cover: File No. 49,385. U. S. Circuit Court of Appeals, Second Circuit. Term No. 932. Trust u/w of Mary Lily (Flagler) Bingham, Messrs. William R. Kenan, Jr., and Lawrence C. Haines, Trustees, Petitioner, vs. Commissioner of Internal Revenue. Petition for a writ of certiorari and exhibit thereto. Filed February 9, 1945. Term No. 932, O. T. 1944.